

AON

M&A and Transaction Solutions for the Healthcare Sector



Tailored Warranty & Indemnity Insurance Solution

Companies within the healthcare sector face a diverse array of risks that require a thoughtful and strategic approach to risk transfer. In 2021 we have seen an upsurge in mergers and acquisitions (M&A) activity across healthcare services and facilities as both sub-sectors continue to consolidate. According to PwC, global deal volumes in health industries increased between 2020 and 2021 by 32% and 65% respectively. Health industries saw increased M&A from Private Equity funds, which accounted for approximately 49% of deal volumes and 54% of deal value in 2021. There has been a 38% increase in FY21 M&A deal volume and a 4.2% increase in M&A deal value.¹

Healthcare organisations require bespoke insurance solutions, including warranty and indemnity (W&I) insurance, to facilitate and support M&A transactions. As the healthcare sector has evolved, so too has insurers' appetite for transactions in the sector. There are now more insurers that will consider underwriting these transactions than in the past. Currently, the biggest hurdle to obtaining comprehensive coverage is the adequacy and thoroughness of diligence.

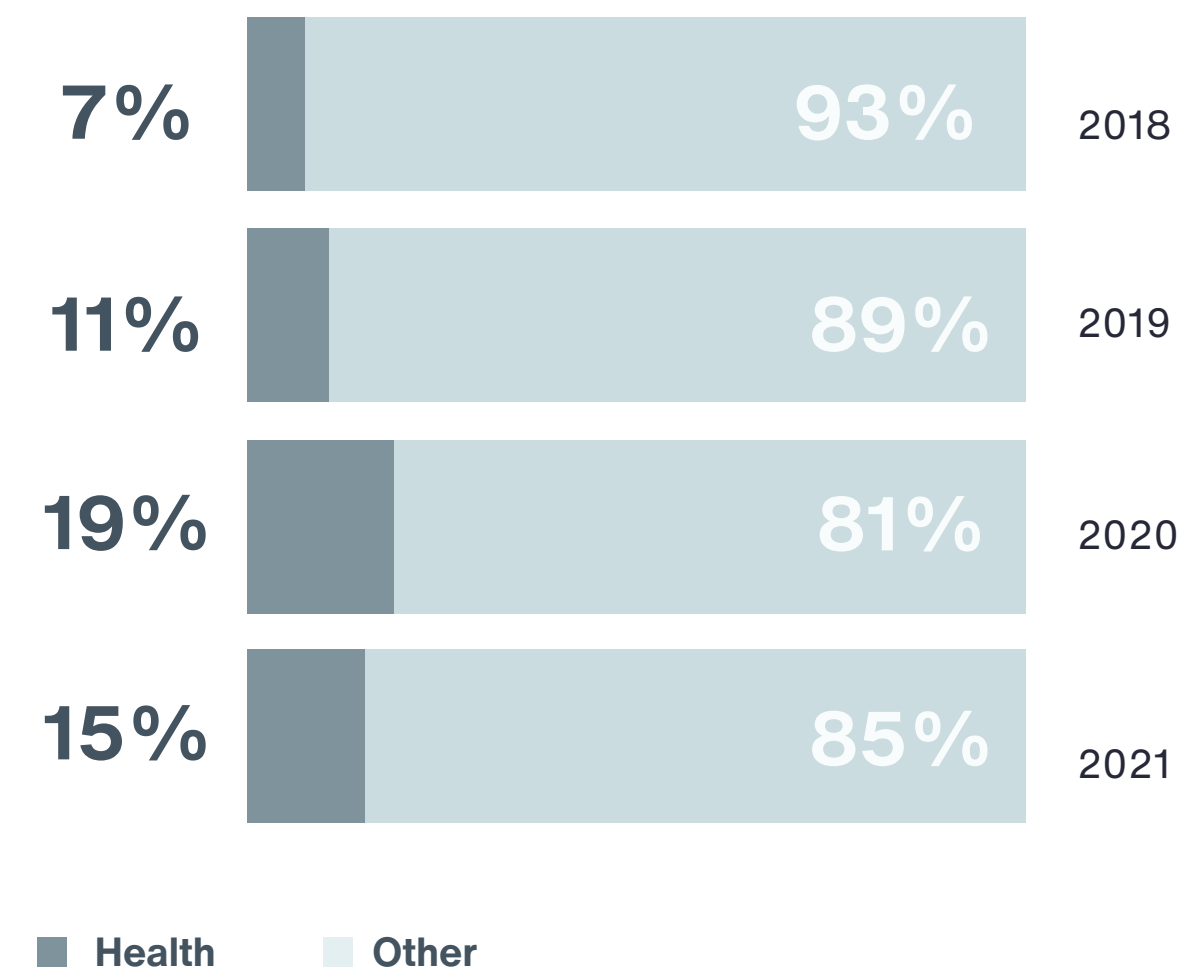
M&A Insurance Market Insights

M&A activity in healthcare services, private hospitals consolidation, clinical research and pharmaceuticals has increased over 2021. We expect this trend to continue into 2022 and beyond with the growth of medical research, biotechnology, biopharmaceutical and life sciences services organisations. There has also been a surge in health-tech transactions including telehealth, biotechnology and medical diagnostic solutions and technologies. In 2021 Aon's M&A and Transaction Solutions team placed over \$390 million worth of insurance in the Australasian healthcare sector.

As illustrated in the graph, deal activity in the healthcare sector has increased since 2018.

We predict a number of factors will lead to a continued increase in M&A activity in the health and aged care sector including Australia's sizeable baby boomer cohort and the recent findings of the Royal Commission into Aged Care Quality and Safety which will likely cause consolidation of aged care facilities.

Percentage of Healthcare Sector Deals



Source: Aon propriety data



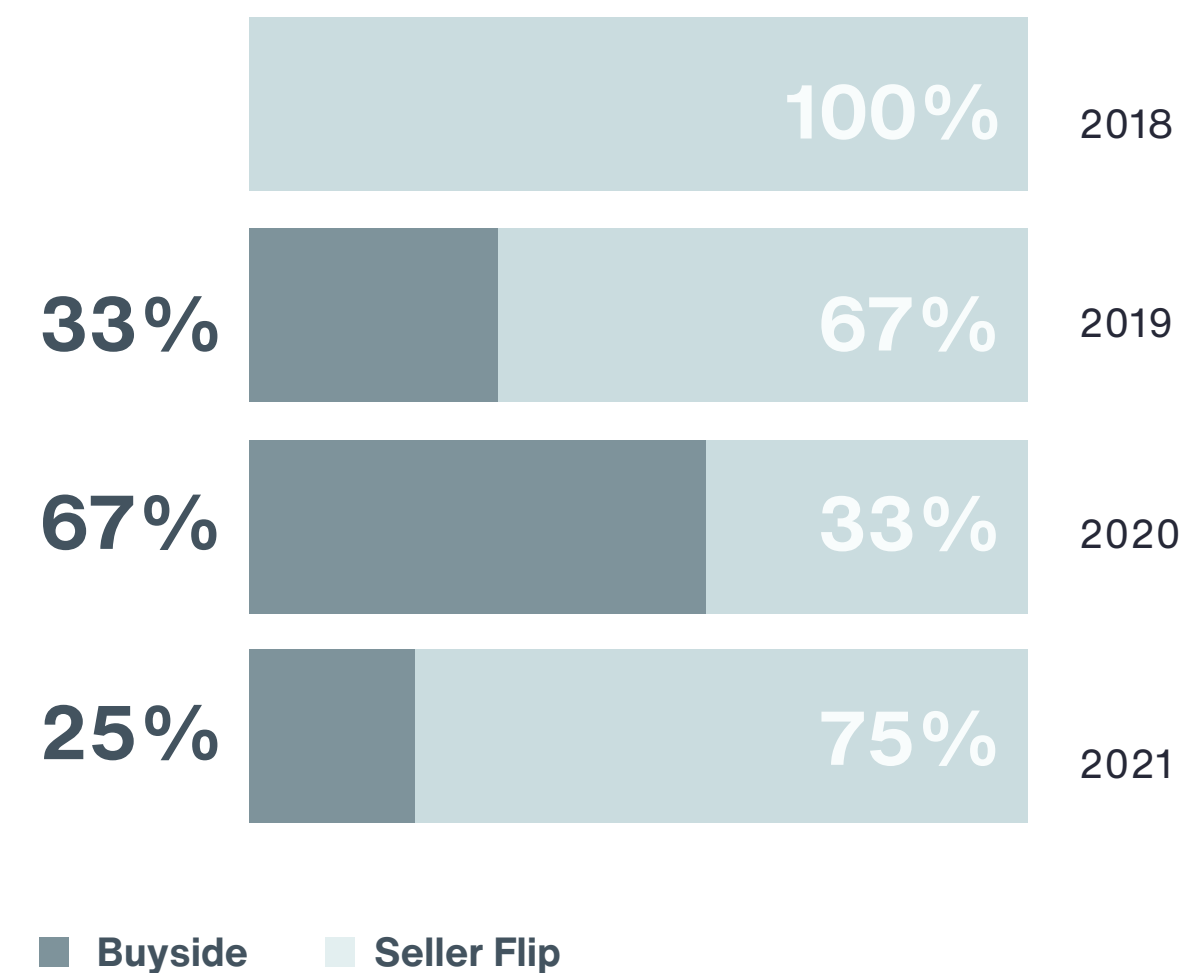
M&A Insurance Market Insights

We have found Corporates and Private Equity funds to be the most active players in the healthcare sector with Corporates typically being international acquirers. In addition, from 2018 to 2021 we have seen sellers tending to opt for a seller mandated process. The rationale for this is that healthcare M&A transactions are usually competitive auction processes with multiple bidders, where the sellers prefer to control the W&I process to ensure unsuitable bidders do not conflict the insurers prematurely. Engaging with brokers at the earliest opportunity on the sell-side is recommended to ensure the chosen primary insurer has sufficient time to complete sell-side underwriting. This means fair and transparent pricing and coverage information can be provided to all bidders at the same time.



Aon placed \$390,200,000 worth of insurance into the health sector in 2021.

Healthcare Sector Sell-Buy Flips



Source: Aon propriety data



How Can Aon Support You in This Market?

Partnering with a risk advisor who has a deep understanding of your business and your industry is critical, especially in an increasingly challenged insurance market.

Aon is a leading provider of insurance broking and risk management services to the Australian healthcare and private hospital sector. Aon's clients represent approximately 85% of the Australian private hospital sector for groups of four or more hospitals. We are also a leading provider of insurance broking services to the aged care, not-for-profit and life sciences sector. This has enabled us to develop specific expertise and to build resources to best service the needs of our clients in these sectors.

Aon's M&A and Transaction Solutions team provides bespoke insurance solutions designed to facilitate and support M&A transactions, including W&I insurance. We work with healthcare organisations across the world to navigate the complexities of the M&A and insurance market.

100s

of clinics and day surgeries

85%

of private hospitals as clients

IVF

Australia's largest IVF businesses

\$47m+

Medical Malpractice premium placed in Australia

No. 1

Supplier of Premium to the top Medical Malpractice insurers – Allied World Assurance Company, Vero, QBE, Dale, and Beazlet

Largest

Australia's largest radiology and pathology businesses

We work closely with our clients, liaising on their behalf with insurers to obtain input on the adequacy of the scope of the diligence being performed. We obtain early indications from the insurers on their focus points, enabling us to help clients navigate the diligence process accordingly.

It is critical clients focus on the quality of the information provided to insurers. To obtain a positive outcome, detailed underwriting is required with good lead time. Engaging early with Aon will increase the probability of favorable terms and coverage while reducing the risk of exclusions.

Key differentiators for Aon in the healthcare sector include:

- **Leverage:** As one of the largest insurance brokers in Australia and New Zealand, Aon is well positioned to place insurance programs in a cost-effective manner, with the broadest possible coverage terms. The sheer volume of premium Aon places into the market on behalf of clients creates negotiating leverage.

- **Experience:** Aon's credentials demonstrate a deep expertise in W&I insurance processes, including experience running highly competitive auctions where it is necessary to manage multiple bidders from diverse jurisdictions.
- **Healthcare Sector Expertise:** Aon has extensive experience working with companies in the aged care, private hospitals, life sciences and clinical research sector and has developed a strong understanding of the risk management and insurance needs in this industry through our dedicated healthcare and life sciences practice groups.
- **Team Credentials:** Aon has a dedicated W&I insurance team in the Australian and New Zealand market, with the majority of members having backgrounds in M&A law. We are complemented by the largest US transactional insurance team of any broker in the Americas, and by dedicated W&I broking team hubs in London, Singapore and Hong Kong.
- **The Aon Client Treaty:** The Aon Client Treaty (ACT) is a unique broking solution available only to Aon clients. It provides an additional 15% of pre-secured Lloyd's insurance capacity to support the placement of large W&I programs.
- **Global Client Base:** In a competitive auction scenario, Aon often transitions from supporting sell side to supporting buy side in the placement of W&I insurance. This is de-risked by the size of Aon's global client base. Many of the bidders in large transactions are typically Aon clients and have an understanding of the quality of Aon's services and our position in the market.
- **Dedicated Claims Resource:** Aon has a dedicated Asia Pacific team of claims advocates who work to deliver the very best results for clients when claims arise. The significant premium volume Aon places into the market also affords Aon considerable market leverage to ensure clients' claims are paid.

Healthcare Warranty & Indemnity Insurance Basic Terms

Below are the basic terms expected on transactions in the healthcare sector.

- Can place up to AU\$1 billion in policy limits.
- Total costs for comprehensive coverage range from 1.5% to 3% of the amount of insurance purchased.
- Retentions (aggregate claims thresholds) are typically 1% of the transaction value and de minimis (per claims thresholds) are typically 0.1% of the transaction value.
- Policy periods can be up to 7 years for title and capacity and tax matters, and 3 years for general operational matters.
- Coverage is provided for a breach of title and capacity warranties, tax warranties and operational warranties including litigation, employment and real estate warranties, and a general indemnity and tax indemnity (if ultimately negotiated in the sale agreement).
- Policy is written by highly rated insurance carriers.



Key Risk Factors

W&I insurance policies have certain limited standard exclusions that W&I insurers will be unwilling to remove, and these generally track concepts in the sale agreement. Aon negotiates the wording of each insurer's template exclusions to ensure they are as narrow in scope as possible on every transaction. These include issues known to the Insured, forward-looking statements, matters included in, or that should properly be included in, any purchase price adjustments (including any earn-outs), consequential loss, certain tax matters such as transfer pricing, secondary tax liabilities, tax losses/anti-avoidance and criminal fines and penalties.



Insurer Areas of Focus

Professional Indemnity/Medical Malpractice/ Defective Products and Services

Insurers closely underwrite to understand how professional indemnity exposures (i.e. liability arising from defective products sold or negligent services by healthcare providers including medical malpractice) are being dealt with at target level. Insurers take the view that professional indemnity exposures should be appropriately covered under professional indemnity insurance.

COVID-19

COVID-19 has altered the risk profile of many transactions in the eyes of insurers. Across Australia and New Zealand insurers have been considering whether to insist on COVID-19 exclusions that have the potential to prejudice the coverage under a W&I insurance policy. However, on recent Australian and New Zealand deals, Aon has successfully negotiated with the insurer to not insist on such an exclusion. It is critical the buyer due diligence stacks up, though we can now ensure advisers are aware of the issues that need to be considered in order for any COVID-19 exclusion to be removed. Once more, we apply competitive pressure up front during our marketing phase to ensure we understand each insurer's intentions with regards to the imposition of a COVID-19 exclusion.

Material Contracts

Insurers closely underwrite to the material contracts that are in place and will focus on ensuring termination rights,

change of control consents, liability provisions of the seller and any unusual or onerous provisions are reviewed as part of the buyer's due diligence.

Cyber/Privacy Risks

With many high-profile cyber-attacks across 2020-21 in most sectors, including healthcare companies, this has become a heightened focus area for insurers. Where a target manages, stores, holds and uses sensitive operating data (particularly patient health records) through infrastructure, insurers have little appetite to cover specific cyber warranties that address breaches of data privacy laws or the occurrence of cyber-related events. Insurers take the view that these risks are more appropriately covered under a cyber policy. Aon will review the adequacy of the target's insurance programs as part of the insurance due diligence and have cyber risk specialists who are available to assist with cyber due diligence.

Employment Matters

Insurers expect a critical review to determine compliance with historical payments of employee obligations. Insurers also expect analysis around compliance in areas such as awards, retirement obligations, employment disputes, policies, casual employment conditions, incentives and industrial agreements. Where there is a large contractor base, insurers and their advisors expect diligence (across a sufficient sample size) to have been undertaken to form a view around the correct classification of employees

and contractors. To gain comfort that the target has been correctly classifying its workforce, insurers typically require sample testing of between 5-10% of the workforce.

Pollution/Contamination

For any business with contamination exposures (either as an owner or operator), regardless of the due diligence undertaken with respect to environmental liabilities, W&I insurers will not provide coverage for the remediation or clean-up of pollution under a W&I insurance policy. Insurers take the view that such exposures are more appropriately covered under environmental liability insurance. The W&I insurance policy will provide coverage for other environmental warranties as to compliance with permits, no known claims, etc. to the extent sufficient due diligence has been undertaken to support these warranties. Aon can assist with the placement of an environmental liability insurance policy.

Insurers have also recently seen an upsurge in claims notifications relating to billing or coding issues that have been triggered by audits or a whistle-blower report. This can result in investigations where a government healthcare scheme is involved such as Medicare.² In addition, pharmaceutical, biotechnology and medical device companies may encounter a number of production-related issues where insurers have seen an upsurge in claims notifications.³ We expect these to be heightened underwriting focus areas for insurers going forward.

Our Experience with Healthcare Sector Assets

Aon has extensive experience arranging W&I insurance for healthcare sector assets. Recent examples include:

- \$1 billion deal in the healthcare sector where we structured a program of \$200 million of W&I insurance.
- \$700 million deal involving a provider of medical solutions and technologies where we structured a program of \$135 million of W&I insurance for the ultimate buyer in a seller-mandated process.
- \$400 million deal in the specialist cancer care services sector where we structured a program of \$75 million of W&I insurance for the ultimate buyer.
- \$400 million deal in the private hospitals sector where we placed \$40 million of W&I insurance for the buyer.
- \$365 million deal involving a business providing clinical trial services where we structured a program of \$225 million of W&I insurance.
- \$327 million deal in the pharmaceuticals sector where we placed \$30 million of W&I insurance for the buyer.
- \$190 million deal in the medical waste sector where we structured a program of \$50 million of W&I insurance.
- \$135 million deal in respect of the sale of several private hospitals where we structured a program of \$30 million of W&I insurance.
- \$53 million deal in the private healthcare facilities and services sector where we structured a program of approximately \$20 million of W&I insurance.



Healthcare Sector Case Studies

Offering the Seller a 'Clean Exit'

Transaction:	\$450 million sale of surgical and day hospitals in Australia and New Zealand to a private equity Buyer.
M&A Risk:	Sellers ran a competitive auction process and sought a clean exit with no residual exposures. There were multiple Sellers involved with the process, many of whom were doctors holding through trust structures. The Buyer wanted traditional protection against post-closing liabilities.
Solution:	Buyer-side Warranty & Indemnity Insurance
Structure:	Limit of 30% of purchase price placed, \$4.5 million retention, equivalent to the Buyer's basket in the underlying sale agreement.
Benefits:	Sellers obtained a clean exit without sacrificing purchase price, enabling expedited returns. The Buyer procured the protection it required to proceed with the transaction. The Sellers and the Buyer were able to negotiate warranties in the sale agreement on an arms' length basis. The transaction was expedited by easing the negotiations between the parties around the scope of warranties and indemnities and related thresholds and caps. The Buyer was also able to take comfort from the Insurer being able to cover the title risk for the various Sellers and their complicated holding structures.



Healthcare Sector Case Studies

Buyer Structuring Greater Protection

Transaction:	\$239 million sale purchase by a private equity firm of a radiology provider.
M&A Risk:	The Buyer wanted traditional protection against post-closing liabilities.
Solution:	Buyer-side Warranty & Indemnity Insurance
Structure:	Limit of 30% of purchase price placed with top up to 100% of cover for title and capacity matters, \$2.39 million tipping to \$1.19 million retention.
Benefits:	The Buyer obtained protection on caps and metrics via the policy which weren't availed of under the sale agreement by the Sellers. The Insurer was able to lower the retention to a tipping retention which is 50% lower than typical retentions offered in the market. The transaction was expedited by easing the negotiations between the parties around the scope of warranties and indemnities and related thresholds and caps.





About Us

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M&A and Transaction Solutions

Aon M&A and Transaction Solutions is a leading provider of specialist due diligence services to the private equity, healthcare and M&A industry. Its capabilities extend across a broad suite of services from risk & insurance, human capital, cyber security and intellectual property. Clients also benefit from its expertise as the largest broker for transaction insurance instruments in Australia and New Zealand including warranty & indemnity, tax, litigation, credit and surety solutions.

For further information on how we secure investments and enhance returns for our clients, please visit: aon.com.au/m&a

Please feel free to reach out and contact any of the team.





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About

Aon plc (NYSE: AON) exists to shape decisions for the better—to protect and enrich the lives of people around the world. Our colleagues provide our clients in over 120 countries with advice and solutions that give them the clarity and confidence to make better decisions to protect and grow their business.

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